# THE REAL CAPITAL CONCEPT.

It is not the purpose of the writer to add another to the already long list of conceptions to which economic literature has given the name "capital." It is his judgment, rather, that there is now in the field a certain conception that is clearly entitled to and should alone bear that name. It is believed that it will conduce to clear thinking, mutual understanding, and sound theory to point out that conception. To this end the present article has been written.

In a former article[1] the writer passed in review the fundamental economic concepts, pointing out certain errors and confusions directly traceable to the lack of a clear apprehension of what he called the fundamental economic principle. He showed that only by keeping the fundamental and universal dependence of man upon the outside world clearly in mind can the basal concepts be defined and the relations of men to each other, in sò far as they are economic, be correctly apprehended. It is essential to note that the dependence of man, on the one side, upon his material environment, on the other, determines not only the beginning and the end of the economic cycle, but gives it direction as well. The wants of man's nature are the motive, the satisfaction of those wants is the goal,—the beginning and the end of the economic cycle. Further, it has been clearly established that the economic cycle embraces, logically, two distinct processes. In Professor Clark's felicitous words,[2] "Man acts upon nature in the one process, nature on man in the other,"—the Production and the Consumption

[1] *Quarterly Journal of Economics*, vol. xv. pp. 218-253.

[2] *The Distribution of Wealth*, chap. ii.

of economic science. A concrete material article, adapted in stuff, form, place, time, and appropriability to satisfy a specific want of man's nature, is, at once, the goal of the one process and the starting-point of the other. To place at man's disposal specific material goods that will satisfy the wants of his nature—his primary economic wants—is, in Professor v. Böhm-Bawerk's phrase, "the end and aim of all production." These economic goods are very properly called "consumption goods" (Böhm-Bawerk),[1] primary goods, or "goods of the first order" (Menger).[2] They comprise all economic goods that minister directly to the wants of man's nature, whether physical, intellectual, æsthetic, spiritual, or moral. They embrace, by way of illustration, all articles that contribute to man's physical health, comfort, and convenience, such as dwelling-houses, articles of food, articles of clothing, house furnishings of all sorts, gymnasia, pleasure horses, carriages, bicycles, automobiles, boats, etc.; art products, such as pictures, statues, and all articles of ornament and adornment; books, newspapers, periodicals, and air products, such as music, speeches, sermons, lectures, etc.

From the standpoint of consumption goods, economic science has fittingly characterized the productive process as direct or indirect,—"roundabout." By the direct method, man puts forth his labor in such a way that the desired article of final consumption "immediately follows the expenditure of the labor."[3] Empty-handed, he wrests from nature the means of satisfying his wants. This is the primitive method. By the indirect method,[4] on the other hand, man directs his labor first towards securing

[1] *Kapital und Kapitalzins*, vol. ii. p. 15.

[2] *Grundsätze der Volkswirthschaftslehre*, chap. i.; "Zur Theorie des Kapitals," in *Jahrbücher für Nationalökonomie und Statistik*, vol. xvii. p. 8.

[3] Böhm-Bawerk, *Kapital und Kapitalzins*, vol. ii. p. 15. [4] Ibid., pp. 16, 17.

an article which, though incapable of satisfying a want of his nature, is still desirable, because with it he can secure the article of final consumption,—if attainable at all otherwise,—at least with a smaller expenditure of labor than he could without it. This "intermediate" article perhaps enables him to utilize some power of nature, or to apply his own labor to better advantage. The indirect method is the method of progress. The goods which satisfy wants that grow out of the productive process itself—secondary economic wants—belong logically to that process, and are appropriately called "production goods" (Böhm-Bawerk), secondary goods, or "goods of a higher order" (Menger).[1] "Production goods," then, comprise, so far as they are devoted to the productive process:—

I. Goods that remain, quantitatively, substantially as determined by nature, embracing areas of land and all natural agents.

II. Goods that may be quantitatively increased or diminished, according to the purposeful, "powerful directing agency of man." This group comprises the so-called "produced means of production," "artificial instruments," in Professor Taussig's phrase "inchoate goods,"[2] the "aggregate of intermediate products," as Professor v. Böhm-Bawerk[3] calls them. To this category of "production goods" belong:—

1. Improvements on land, so far as these are designed to aid in the productive process; for example, dams, drains, fences, etc.

2. Buildings of all sorts for the furtherance of production; for example, workshops, factories, barns, shops, streets, railroads, theatres, school-houses, churches, court-houses, etc.

[1] "Zur Theorie des Kapitals," *Jahrbücher für Nationalökonomie und Statistik*, vol. xvii. p. 8.

[2] Taussig, *Wages and Capital*, New York, 1896, pp. 36, 37.

[3] *Kapital und Kapitalzins*, vol. ii. pp. 15–23.

3. Tools, machines, and all sorts of productive instruments and utensils.
4. Draft animals.
5. The raw and auxiliary materials of production.
6. Stocks of consumption goods still in warehouse and shop.
7. Money.

It is evident that the distinction between *production goods* and *consumption goods is fundamental,* that the classification is comprehensive and the nomenclature scienticallly adequate. All economic goods belong, either logically according to their nature or by assignment on the part of man, to the one or the other of these two classes. To confound them is to render clear thinking impossible.

Professor v. Bőhm-Bawerk[1] has very appropriately called production by the indirect method "capitalistic production," as opposed to that method "which goes directly at its object." It is certainly true that the employment of "intermediate products" is one of many outward manifestations of the existence of capital. Specialization is another. These phenomena and many others rest upon a *common foundation,* which alone makes it possible to put a more or less protracted interval between the beginning and the end of the productive process. Our proposition is that the term "capital" should be applied to this *underlying basis* of the "roundabout" method of production rather than to any one of its specific outward manifestations. There is little room for doubt that Jevons[2] had had a glimpse of the essential truth of this proposition when he wrote, from the standpoint of the productive process, "The single and all-important purpose of capital is to enable the laborer to await the result of any long-lasting work,—to put an interval between the beginning and the end of an enterprise."

[1] *Kapital und Kapitalzins*, 1884, 1889, vol. ii. p. 21.

[2] *The Theory of Political Economy*, London and New York, 1891, p. 214.

Let us ask ourselves directly, What is this underlying basis of "capitalistic production" that seems so clearly entitled to bear the name "capital"? The answer might be made in the words of Professor Hearn:[1] "If there were no accumulated fund upon which the laborer could rely, no man could remain for a single day exclusively engaged in any other occupation than those which relate to the supply of his primary wants." But, to make the answer more direct, it is *surplus wealth as a possession: capital is surplus wealth as a possession.* Without it there could be no tools, machinery, factories, dams, workshops, and improvements on land; there could be no specialization, with all its marvellous increase of productive power; there could be no leisure, no science, no purposeful employment of the power forces of nature; there could be no borrowing and loaning; man would be still engaged in a hand-to-hand struggle with nature for the bare necessaries of life. In short, there would be barbarism, with no possibility of progress. It is capital, in the sense of *surplus wealth as a possession,* that places man in a condition favorable to progress, and enables him to secure the means of improvement. The primary agencies in production remain to-day, as in the beginning, man and nature. Yet capital, in the sense of *surplus wealth as a possession,* has enabled man to acquire such a knowledge of and command over his own powers and the forces of nature, such a prerequisite has it become to every industrial undertaking, that economists have been led to recognize it as a distinct factor in production, co-ordinate with man and nature.

The definition of capital as a fund of *surplus wealth as a possession* reveals at once that capital and wealth are not synonymous terms. Wealth is the broader, capital the narrower, of the two concepts. Unfortunately, it is necessary here to explain what is meant by wealth. The

[1] *Plutology,* London, 1864, p. 140.

writer has elsewhere[1] traced the evolution of the wealth concept. He has pointed out that the term "wealth" has always signified the relative weal-relation of the individual to his material environment; that it meant originally a condition of relative well-being, but came to be used in time, by a transfer of meaning, to signify that which creates the condition; that when the productive process was individualistic, when there was no organization and no exchange of products, a person's wealth signified the economic goods he owned, roughly estimated for the purpose of comparison in terms of area, weight, or number, while to-day, with a social productive process, a system of exchanges, and a money economy, a person's wealth signifies no longer the concrete economic goods, but, rather, the *quantum of social value* he owns, and is always expressible in terms of money. It is practically necessary in estimating a person's wealth, then, to have an inventory of all the economic goods he owns, and to add to the carefully determined social value of the same the amount of all good claims and to subtract the amount of all debts. The terms "property," "assets," "liabilities," and "wealth" designate well-defined and familiar phenomena in practical life and in jurisprudence.

To return now to our definition of capital as *surplus wealth as a possession*, it is evident that the capital concept has undergone an evolution parallel with that of the wealth concept. When a person's wealth signified, as it did in primitive times, the aggregate of the economic goods that

[1] *Annals of American Academy of Political and Social Science*, vol. i. pp. 615–634; *Quarterly Journal of Economics*, vol. xv. pp. 237–242.

The term "wealth," far from being the "popular expression for goods the exact valuation of which is not stated," always implies measurement and exact statement in terms of the unit of value. This is the concept which the term signifies, when used in the strictest accordance with etymology and popular speech. The writer has emphasized in an article in the *Quarterly Journal of Economics*, vol. xv. pp. 237–242, in the interest of sound theory, the importance of retaining the two conceptions of wealth and economic goods,—the one abstract and the other concrete. See article by Professor Fetter in *Quarterly Journal of Economics*, vol. xv. pp. 42–45.

belonged to him, roughly estimated for the purpose of comparison in terms of area, weight, or number, capital in the sense of *surplus wealth as a possession* signified an accumulated store of goods over and above what was required for the satisfaction of current wants. The *store* of dried fish that Walker's primitive fisherman takes out into the hills to live upon while he constructs a boat is an illustration in point. The distinction is made between the *store* and the dried fish that the man requires for current consumption. The fisherman's wealth includes *both;* his capital, only the *former*. Dried fish as they are applied, day by day, to the satisfaction of current wants vanish; but the *store* does not disappear, if the man has been industrious as a boat-builder. When the *fish* are gone, the *store* still exists in the form of a boat. But to-day, with a social productive process, a system of exchanges, and a money economy, when a person's wealth consists not in the economic goods, but, rather, in the *quantum* of social value he owns, his capital in the sense of *surplus wealth as a possession* signifies a surplus *quantum* of social value expressible in terms of money. Our definition, then, is as follows: *capital is surplus wealth as a possession, expressible in terms of money.*

It is evident that a person may have wealth and not, at the same time, possess capital. In that case he must have lived from hand to mouth, must have expended his income currently as he received it, has accumulated no surplus. To have capital, as John Stuart Mill[1] would put it, he must have consumed less than he produced or produced more than he consumed. A person's *wealth* is the total *quantum* of social value that belongs to him; while his *capital* is what is left after deducting the amount required for current consumption. Employing the term in this sense, it is evident that "saving, self-denial and

[1] *Principles of Political Economy*, vol. i. chap. v. § 4.

abstinence," are factors in capital-building. Capital originates in a surplus: it grows through surplus accumulation. There is no mystery about the origin and growth of capital. It is naturally easier for some men to accumulate capital than for others. It is easier for the man of large productive capacity and large self-control than for the man of small productive capacity and small self-control. It is easier, other things remaining the same, for the man of foresight than for the improvident, for the selfish man than for the generous, for the unmarried man than for the married, for the man of small family than for the man of large family. Some men seem to have a genius for capital-building; while others are, seemingly, utterly devoid of capacity in that direction. There is no monopoly of capital-building: the opportunity is open to every man who is capable of meeting the conditions.

It is important here to emphasize the fact that capital according to our conception is not money, though it is always expressible in terms of money. A portion of one's capital or all of it, for that matter, may be momentarily in the form of money. Ask a business man, How much capital have you? his answer may be, I have fifty thousand dollars: it will certainly be in terms of money, though he may not possess at the time one dollar in actual coin.

It is equally important to note that capital, according to our conception, is not land, buildings, machines, materials, or workshops. The distinction between a thing and its value must be kept always in mind. Capital is not a concrete material article. Specific economic goods —a McCormick reaper and binder, for example—cannot be expressed in dollars and cents. Economic goods may serve as an investment for capital, but they are not capital. By way of illustration, take a given horse: its value is five hundred dollars, its weight two thousand pounds,

its height seventeen hands. Who would say that the horse and its weight or its height or its value were one and the same thing? As the weight of a horse is the measure of one physical property, and the height of another, so the value is the measure of the economic quality of effective utility. Capital, then, is a fund of value,—*surplus wealth as a possession,*—and not a material product or an aggregate of such products.

The writer firmly believes that he has found the real capital concept, and in support of this claim would call attention to the following considerations:—

1. The conception capital in the sense of *surplus wealth as a possession,* expressible in terms of money, is the common practical conception of capital.

This is a fact of prime importance. Economic science treats of the business world. Its terms are largely terms of popular speech. The scientific concepts to which these terms are applied should be determined, it seems hardly necessary to observe, by the analysis of the corresponding popular notions. Otherwise, our science will arouse distrust in and be unintelligible to the popular mind. In popular speech, capital signifies a loan fund: the capitalist is the man who possesses loanable wealth; or, in the words of popular speech, "the capitalist is the man who has money at interest or money to loan." It is clear that no man can have a loan fund or loanable wealth, or, in popular phraseology, "money to loan" or "money at interest," unless he is the *owner of surplus wealth,* as we have defined it.

Further, in popular speech, capital is always expressed in terms of money. Ask a merchant, a manufacturer, or a banker, What is your capital? the answer will invariably be in terms of money. A man or a company, to go into business, must have a certain amount of capital. The amount is always given in terms of money.

Again, in business life, interest is the peculiar form of income which attaches to capital. The capitalist alone is entitled to interest, and the law recognizes and protects his right. The owner of buildings, machines, workshops, and materials, is not, as such, either economically or legally entitled to interest. Only the owner of the invested fund of capital expressed in terms of money can economically claim interest, and the law recognizes the claim. Interest is always expressed as a percentage upon a fund of value. To quote Professor Clark,[1] "It has no reference to the form in which the capital is invested: a thousand dollars per annum is interest on twenty thousand, whether that larger sum be, for the moment, invested in ships, farms, or merchandise." The peculiar form of income which the owner of concrete instruments—whether land, buildings, or machines—is economically entitled to is called, in the business world, rent; and, again, the law recognizes his title. It often and indeed commonly happens, in these days of credit transactions, that the owner of the capital is not at the same time the owner of the instruments in which his capital is invested: he may not own a foot of land, a building, or an implement. He loans his capital to another, who invests it in land, buildings, and machines, and stands before the law as the owner of these instruments. While the former (the capitalist) is economically and legally entitled to interest,—the earnings of capital,—the latter (the business owner) is entitled to rent,—the earnings of instruments. It is one of the hopeful indications that economic science is coming into closer touch with the practical world, that economists to-day no longer limit the term "rent" to the earnings of land, but have extended it to the earnings of all concrete instruments. Has not the time come to restrict the applica-

[1] *Capital and its Earnings*, Publications of American Economic Association, vol. iii. p. 106.

tion of the term "capital" to the conception of *surplus wealth as a possession,* expressible in terms of money, thus bringing our science still further into harmony with actual business life?

The position of Professor Carver,[1] that value measurements are in reality measurements of the instruments, and that "the instruments are the capital, and the amount of value in them is not the capital," seems to the writer to be entirely disproved by the discriminations of practical business life. The aggregate of specific production goods of varied technical character is not a sum, but an inventory. On the other hand, simple addition may be applied to the *value* of such goods if expressed in a common denominator. A sum of production goods of varied technical character is meaningless. One cannot jumble together bushels of wheat, sacks of wool, tons of coal, barrels of gasoline, and electric motors, and express the result by a single figure.

2. Etymology appears to show that our conception of capital is the true one, and is clearly entitled to bear the name.

It is now sufficiently well known that the word "capital" was used in ancient and mediæval times in the abstract sense. It signified a fund of value, a quantity of surplus wealth. It was spoken of in terms of money, as a capital of so many pounds, louis d'or, florins, and what not. It brought before the mind, not a picture of a heap of coin, or of buildings, tools, materials, or finished goods, but rather a picture of a certain purchasing power, a certain command over commodities in general. It was exactly what we think of in practical life to-day when we are told that a corporation has a capital of a million dollars. It seems to be clearly established[2] that the term "capital"

1 "Clark's Distribution of Wealth," *Quarterly Journal of Economics*, vol. xv. pp. 587-592.

2 Knies, *Das Geld*, Heidelberg, 1873, pp. 6-7; Böhm-Bawerk, *Kapital und Kapitalzins*, vol. ii. (1889) p. 23; Irving Fisher, "What is Capital?" *Economic Journal*, vol. vi. p. 517.

has come down to us, through the mediæval *capitale*, from the Latin *caput;* that it signified originally the principal of a money loan, as distinguished from the interest. The *capitalis pars debiti* was the principal of a debt. It was that part which it was of vital or "capital" importance to preserve intact, as opposed to interest which might be spent with impunity. Now a loan fund is essentially nothing more nor less than *surplus wealth as a possession.* He who *possesses surplus wealth* has a fund that he can loan. Money was, and still is, the most convenient form in which a loan could be effected. The nature of capital is fundamentally the same, whether it be made the basis of a credit transaction or be applied directly to production. The specific use to which it may be put does not affect its real character.

The prohibition of interest by the church authorities and the *Canon Law* led to the discovery that the interest-bearing power of money lay in the earning capacity of the things bought with it. It was believed that the man who loaned money virtually loaned tools, materials, etc. This idea is brought out clearly by Hume[1] in his essay on *Interest.* The English word "capital" and its Continental equivalents retained essentially the mediæval signification down to the time of Turgot. Yet there is evidence as early, at least, as the middle of the seventeenth century that the total value of a merchant's estate expressed in terms of money, as distinguished from the "wares," "commodities," or "parcels" in which it is contained, was sometimes called a capital.[2] There was manifestly a tendency to extend the conception of capital beyond the bounds of the principal of a money loan.

3 Our conception of *surplus wealth as a possession* is

[1] *Essays, Moral, Political, and Literary*, vol. i. pp. 321, 322.

[2] Gerard de Malynes, *Consuetudo vel Lex Mercatoria, or The Ancient Law Merchant*, London, 1656, Part Second, chap. xx. pp. 241-250.

clearly entitled to be called capital according to the four leading principles which Professor v. Böhm-Bawerk, who regards the capital controversy as essentially one of terminology, lays down to be observed in such cases. These principles are formulated as follows:[1]—

> First, and chiefly, it is self-evident that the construction of the proposed conception must be logically unassailable; that is, it must not contradict itself and must cover the object which it is proposed to define.
>
> Then there should be no waste of terminology; that is, the name "capital" should not be applied as a synonym to a conception already named.
>
> Third, the selected conception must, further, be scientifically important and fruitful.
>
> And finally, fourth, the name "capital" must be left for that conception for which it has been longest and most generally used.

The application of these principles to the conception under consideration leaves no doubt as to its claim to the name "capital." The construction of the conception certainly does not contradict itself, and adequately covers the object which it is proposed to define; there is no waste of terminology in applying the name "capital" to this concept; the concept is scientifically important and fruitful; and, finally, it is the conception which has been longest and most generally called capital. Says Professor Clark,[2]—

> This abstract conception of capital is employed in business a hundred times where the concrete conception is employed once. For the purposes of a scientific study of modern problems, it is the primary notion of capital. . . . The actual practice of economic science has been to first define capital in the concrete and then, in the problems connected with it, to tacitly substitute again and again the abstract conception.

Every careful student of the literature of capital can testify to the truth of this indictment that hangs over our

[1] *Kapital und Kapitalzins*, vol. ii. (1889) p. 38.

[2] *Capital and its Earnings*, Publications of American Economic Association, vol. iii. pp. 11–12.

science. Even Professor v. Böhm-Bawerk is not free from the charge, Professor Fetter's well-founded criticism of Professor v. Böhm-Bawerk's treatment of capital is

> that, while defining capital as if it could be spoken of without reference to value or the use of value expressions, he employs a value concept almost entirely in his reasoning on the interest problem. He makes a shift without being conscious of it.[1]

Although the idea of *surplus wealth as a possession*, expressible in terms of money, clearly underlies the ancient and mediæval conception of capital, Turgot was the first economist to give it full and conscious recognition.[2] He not only made it his conception of capital, but gave it a place in the literature of economic science. In Section 59 of his *Réflexions sur la Formation et la Distribution des Richesses* he expresses himself as follows:—

> Whoever either from the revenue of his land, or from the wages of his labor or of his industry, receives each year more value than he needs to spend, can place this surplus in reserve and accumulate it: these accumulated values [*valeurs accumulées*] are what is called capital.[3] . . . It is a matter of absolute indifference whether this sum of values, or this capital, consists in a mass of metal or anything else, since money represents every kind of value, just as every kind of value represents money.

Again he says in Section 100:—

> In fact, almost all savings are made in nothing but money. It is in money that the revenues are paid to the proprietors, that the advances and the profits return to entrepreneurs of every kind: it is therefore from money that they save, and the annual increase

[1] "Recent Discussion of the Capital Concept," *Quarterly Journal of Economics*, vol. xv. p. 40.

[2] Professor Taussig says of Turgot's theory of capital that it "may justly be called the first modern discussion of the subject." *Wages and Capital*, p. 127.

[3] Professors Knies and v. Böhm-Bawerk have seemingly misinterpreted Turgot's definition of capital. They translate it as *diese angehäuften Güter*. Knies, *Das Geld*, p. 9; Böhm-Bawerk, *Kapital und Kapitalzins*, vol. ii. p. 24.

of capital takes place in money; but none of the entrepreneurs make any other use of it than to convert it immediately into the different kinds of articles upon which their undertaking depends. Thus this money returns to circulation, and the greater part of capital exists in articles of different kinds.

Capital, then, according to Turgot, is surplus wealth as a possession, expressible in terms of money: it does not embrace all wealth, but only a portion of it; it is not money, but is expressed in terms of money; it is the result of saving, and money is the form in which it is accumulated. Though it may be loaned at interest, it has other uses. Turgot[1] enumerates and comments upon five different uses to which capital may be profitably put. It may be invested in land, in agricultural undertakings, in industrial or manufacturing undertakings, in commercial undertakings, or it may be loaned at interest. Thus capital, according to Turgot, finds investment in all kinds of production goods comprised under land and the "aggregate of intermediate products"; but it is to be found also in those consumption goods[2] which last for some time, while they admit of being used,—durable consumption goods. The use—usance—of such goods is the article of current consumption; while the good itself represents an investment of capital. Turgot mentions dwelling-houses, furniture, jewels, plate, paintings, and statues. It is not necessary to own such articles in order to have the want satisfaction which their use affords. Turgot's position is unassailable. It is evident that he who owns no capital, in the sense of *surplus wealth as a possession,* and cannot borrow, cannot own a house, a horse, a piano or an automobile; but he may be able to pay currently for the use—usance—of these things, and his wants may be as well satisfied as they would be in case he were the

[1] *Réflexions sur la Formation et la Distribution des Richesses,* §§ 59–89.

[2] Ibid., § 91.

owner. He who owns, free from debt, a house worth five thousand dollars, has five thousand dollars capital according to Turgot's conception, whether he himself consumes the usance of the house or sells it to another. He who owns, free from debt, a piano worth five hundred dollars has a capital of five hundred dollars, whether he uses the piano for his own pleasure or as a teacher, or rents it to another. It is a matter of indifference to what use the concrete article may be put: if it lasts for some time while it admits of being used, its value is capital, in the sense of *surplus wealth*, to the owner, and may be loaned or consumed or reinvested at his pleasure. When Turgot speaks of capital as a "mass of values saved and accumulated" or as "a sum of money,"[1] there can be no doubt of his meaning. *Surplus wealth as a possession*, expressible in terms of money, irrespective of what it may be invested in, is capital. He correctly speaks of capital, in this sense, as "the indispensable foundation of every undertaking."[2] It takes its place by the side of man and nature as a distinct agency in production, has revolutionized the productive process, given it its name, and opened up boundless possibilities of progress.

The side-tracking of the Turgot capital concept by Adam Smith, and the substitution upon the main track of economic discussion of a brand-new concept, were fraught with serious consequences for the theory of capital. Perhaps the most unfortunate feature of Adam Smith's treatment is the apparent assumption that the thing which in political economy is called capital is not open to question, so that all one has to do is to declare that this and this is capital. The idea of a surplus, which with Turgot was the fundamental characteristic of the capital concept, becomes with Adam Smith the distinguishing feature of

[1] *Réflexions sur la Formation et la Distribution des Richesses*, § 68.
[2] Ibid., § 71.

"stock." Yet the two concepts were by no means identical. While Turgot's capital was a fund of surplus wealth, expressible in terms of money, Adam Smith's "stock" is an accumulation of concrete goods. In other words, Turgot's capital is invested in Adam Smith's stock. But, with Adam Smith, "stock" and capital are not synonymous terms: on the contrary, a man's stock is

> distinguished into *two parts*. That part which, he expects, is to afford him his revenue, is called his *capital*. The other is that which supplies his immediate consumption, and which consists either, first, in that portion of his whole stock which was originally reserved for this purpose; or, secondly, of his revenue from whatever source derived, as it gradually comes in; or, thirdly, in such things as had been purchased by either of these in former years, and which are not yet entirely consumed, such as a stock of clothes, household furniture, and the like.[1]

According to this, Adam Smith's conception of capital comprises a category of concrete goods, and is based upon a distinction between goods designed for the purpose of acquisition and those reserved for personal consumption. He immediately shifts his position, however, and marks off, on the basis of productivity, a smaller category of goods—production goods—which he thinks especially entitled to be called capital,—national capital,—and thus excludes a long list of goods which have an income-earning power, on the ground that they "cannot yield any to the public, nor serve in the function of a capital to it, and the revenue of the whole body of people can never be in the smallest degree increased" by them, though they may yield a revenue to their owner. After thus placing especial emphasis upon productivity as a characteristic of capital, Adam Smith proceeds to specify the different kinds of production goods which as fixed and circulating capital belong to the category of capital.

[1] *Wealth of Nations*, vol. i. Book II. chap. i.

The assumption by so commanding an authority as the "father of political economy," *first*, that capital consists of a category of concrete goods, and, *second*, that the acquisition of income or productivity is the decisive element in the capital concept, is the historical source of the disagreements, confusions, and logomachies that followed. A false trend was given to the theory of capital. Jevons might "protest against deference to any man, whether John Stuart Mill or Adam Smith or Aristotle, being allowed to check inquiry";[1] but he was unable to throw off the spell. As the assumption that wages are paid out of capital turned the discussion of wages from the right track, so the assumption that capital consists of a category of concrete economic goods devoted to acquisition or, more specifically, to production has vitiated the discussion of capital. The main purpose of Adam Smith's successors seemed to be to determine what goods belong to the category of capital and what do not. From time to time the discussion seemed to focus upon certain points, which remain still centres of controversy. The following will be recognized as such:—

1. Are "the acquired and useful abilities of all the inhabitants or members of society" capital, on the ground stated by Adam Smith,[2] that "the acquisition of such talents . . . always costs a real expense, which is a capital fixed and realized, as it were, in his [the laborer's] person"? If so, then J. B. Say and John Stuart Mill are right, that the laborer[3] himself is an investment of capital, and Roscher, that the state[4] is capital; and the fundamental and universal economic principle of the dependence of man, on

[1] Jevons, *The Theory of Political Economy*, London and New York, 1891, pp. 270–275.

[2] *Wealth of Nations*, vol. i. Book II. chap. i.

[3] J. B. Say, *Cours Complet d'Économie Politique Pratique*, vol. i. p. 316; Mill, *Essays on Some Unsettled Questions*, pp. 87, 88.

[4] Roscher, *Die Grundlagen der Nationalökonomie*, p. 81.

the one side, upon his material environment, on the other, is obscured, and correct reasoning is rendered impossible.

2. Are durable consumption goods, like dwelling-houses, furniture, pianos, and what not, capital, as Adam Smith suggests, in case they are employed as a means of acquiring an income? If so, Professor v. Böhm-Bawerk's conception of capital in the broader sense—"private or acquisitive capital"—is correct, though it ignores the fundamental distinction between *consumption goods* and *production goods*, separates the like and brings together under one category the unlike, compelling us to say, as Professor Fetter has put it,—

> that a thing becomes capital or ceases to be capital not because of any change in its physical or economic nature, not because it is more or less serviceable to the community, not because the use to which it is put is altered, but simply because the man who owns it does or does not happen to be the one who enjoys that use.[1]

3. Shall land be included under the category of capital, as Hermann[2] proposes, on the ground of its being "a good which continues to exist while it yields an income" and occupies the "first place among goods that are necessary to production"?

Adam Smith did not so include it, and the majority of writers since have followed in his footsteps. Professor Menger[3] has, however, clearly shown that its exclusion was arbitrary. It grew out of an attempt, not to find a scientific definition of the concept, but rather to give the name "capital" to the third requisite of production in the triad of "land, labor, and capital," corresponding to the third form of income from production in the triad of "rent

[1] Fetter, "Recent Discussion of the Capital Concept," *Quarterly Journal of Economics*, vol. xv. p. 23.

[2] *Staatswirthschaftliche Untersuchungen*, München, 1832, p. 48.

[3] "Zur Theorie des Kapitals," Conrad's *Jahrbücher für Nationalökonomie und Statistik*, vol. li. pp. 11–29.

of land," "wages of labor," and "interest on capital." Land, though belonging to the category of production goods, was excluded from capital, ostensibly, on the ground of its origin. It is described as a "gift of nature," while capital comprises only those goods which are "products" of labor. Definitions were framed, accordingly, for the express purpose of excluding land, as, for example: capital comprises the "produced means of production," the "aggregate of intermediate products" (Böhm-Bawerk), "artificial instruments of production" as opposed to "natural instruments." On the other hand, it has been clearly demonstrated that these definitions do not logically exclude land. If labor when applied to wood or iron creates a "product," why does it not equally create a "product" when applied to land? Yet economists attempt to distinguish between land and "improvements on land," excluding the former from the category of capital on the ground that it is not a "product," though they make no attempt to distinguish between wood or iron and the improvements upon them.

4. Again, "is there any capital that is simply a fund for the maintenance of labor"?

He who defines capital as a category of "production goods,"—"instruments of production,"—such as tools, machines, buildings, and raw materials, cannot logically enumerate, as a form of capital, the "food of the laborer." Yet "subsistence" is represented as the earliest form of capital, co-ordinate with tools and materials which come later. Though it has been repeatedly pointed out that articles of food are consumption goods, and can therefore, in no proper sense, be regarded as "instruments of production," yet, with a persistence that would not be put down, a long succession of economists, beginning with Adam Smith and including the most distinguished names—English, French, German, American—in economic liter-

ature, have continued even down to the present day to regard a "fund for the maintenance of labor" as a form of capital. Yet even here the instincts of men are a guide to scientific truth: it is the definition that is wrong.

A recent writer[1] has proposed to "pour oil upon the troubled waters" by employing the term "capital" to comprise "all commodities in existence at any particular instant." According to Professor Irving Fisher,[2] a "full view of capital would be afforded by an instantaneous photograph of wealth" (economic goods):—

> It would disclose, not the annual procession of such goods, but the members of that procession that had not yet passed off the stage of existence, however swiftly they might be moving across it. It would show train-loads of meat, eggs, and milk in transit, cargoes of fish, spices, and sugar, as well as the contents of private pantries, ice-chests, and wine-cellars. Even the supplies on the table of the man bolting his dinner would find a place in our flash-light picture. So also the clothes in one's wardrobe or on one's back, the tobacco in a smoker's pouch or pipe, the oil in the can or lamp, are capital.

This conception certainly has the merit of doing away with the futile attempts to classify economic goods into capital and non-capital, for it embraces them all indiscriminately. It is free from the error of regarding acquisition or productivity as the decisive element in the capital concept. As Professor Fisher[3] explains:—

> We are no longer called upon to mark off sharp distinctions between goods which are "productive" and "unproductive," "intermediate" and "enjoyable," "durable" and "perishable," for "supporting laborers" and for "unproductive consumption," nor are we constrained to enter into sophistical disputes as to whether the distinction between capital and other wealth (economic goods)

[1] Irving Fisher, "What is Capital?" *Economic Journal*, vol. vi. pp. 509–534; Hadley, *Economics*, New York, 1896, pp. 5, 6.

[2] "Senses of Capital," *Economic Journal*, vol. vii. p. 199. Fisher uses the term "wealth" in the sense of economic goods.

[3] *Economic Journal*, vol. vii. pp. 199, 200.

lies in "the nature of the goods" or in the "intention in the mind of the capitalist," or whether rented dwellings may be capital to society as well as to the owner, or whether land and natural agents can be separated from their improvements.

But why apply to the so-called "stock" of economic goods in existence at a given instant the name *capital?* To this question Professor Fisher has not given a convincing answer. One excuse the author gives is the "perpetual collapse of proposed definitions, which suggests that the foundations have not been properly laid." He finds,[1] "beginning with Adam Smith, that every definition of capital has been erected on the unquestioned assumption that the problem was one in the classification of wealth" (economic goods). He, therefore, proposes to broaden the foundation of the capital concept by making it embrace all economic goods in existence at a particular instant of time.

That the distinction between "a stock" and "a flow" or "a rate of flow" is an important one, the writer of this article does not doubt. But he can find no justification in etymology or "in history or in popular and business usage" for the application of the term "capital" to such "a stock." The conception is adequately and scientifically characterized by the phrase, "the existing stock of economic goods at an instant of time." To apply the term "capital" to it is not only confusing, but arbitrary and wasteful of terminology.

It is important to note that Professor Fisher's conception of a "stock" is much broader than that of Adam Smith. To the latter the *idea of a surplus* is the fundamental characteristic of stock, while to the former "stock" comprises all economic goods in existence at a given instant. To illustrate, while to Adam Smith, on the one hand, "stock" corresponds to the pond of water,—the

[1] "What is Capital?" *Economic Journal*, vol. vi. p. 513.

accumulated surplus of the inflow over the outflow,— to Professor Fisher, on the other hand, it is the pond of water plus the water in the inflowing and outflowing streams at an instant of time. Yet, in spite of his definition, Professor Fisher unconsciously lapses into Adam Smith's conception of "stock." He does this when he illustrates that his distinction between a "stock" and a "rate of flow" "brings capital into the simplest and most intimate relation to interest."[1] He says: —

> When a stock of goods or capital is exchanged for a perpetual flow of goods or income, the ratio of exchange constitutes the rate of interest. If £100 will buy an income of £3 per year or if 100 tons of beef are worth a perpetual supply of three tons annually, the rate of interest is three per cent. per year. [1]

What makes it possible, we ask, to exchange £100 for an income of £3 per year? Is it *simply* the fact that £100 is in "existence at a given instant of time"? Certainly not: it is because £100 exists under such conditions that it is possible to use it to buy an income. In other words, it must exist *as a surplus*. Again, when Professor Fisher[2] states that his idea of capital is deeply rooted in the minds of economists themselves, and by way of illustration quotes from Adam Smith the expression, "By not confining his expenses within his income, he [the prodigal] encroaches on his capital," he has evidently misinterpreted the passage. There is no room for doubt that Adam Smith, in the above passage, uses the term "capital" in the *sense of a surplus* of some sort.

Space forbids the multiplication of illustrations. Suffice it to say that Professor Fisher, in avoiding the error of regarding acquisitiveness or productivity as the all-

[1] Fisher, "What is Capital," *Economic Journal*, vol. vi. p. 515.

[2] "The Rôle of Capital in Economic Theory," *Economic Journal*, vol. vii. p. 537.

important characteristic in the capital concept, has proposed not only to drop from the concept the truly fundamental element,—the idea of a surplus,—but to perpetuate the erroneous assumption of Adam Smith that capital consists of concrete economic goods.

The profound German theorist and critic, the late Professor Karl Knies,[1] has subjected the controversy which grew out of Adam Smith's discussion of capital to a searching critique, and brought out prominently the fundamental nature of the capital concept. He showed as conclusively as it is possible to show, admitting the validity of Adam Smith's assumption that capital consists of a category of concrete goods, that the fundamental and all-important element in the capital concept is the *possession* (*Haben*) of an *accumulated stock* of goods. He pointed out that men are called capitalists or non-capitalists, large capitalists or small capitalists, on the basis simply of the *possession of a stock of goods*, and without reference to the particular way the goods are used; that the same man may own a herd of cattle on one day, houses on the next, on the third sums of money, and an art gallery on the fourth, and each day be a capitalist. It seems unaccountable that Professor Knies did not discover the error of Adam Smith's assumption, as in these days of credit transactions men are not accounted capitalists at all on the basis simply of the possession of a stock of goods. The possession of a fund of surplus wealth expressible in terms of money is, rather, the decisive element. With convincing logic, admitting again the validity of his assumption, Professor Knies asserts that the conception of a stock of goods as a possession should be investigated in all its bearings and fully understood, apart from and preliminary to any specific use to which it may be put. His conception of a stock of goods is seemingly identical with that

[1] *Das Geld*, Berlin, 1873, chap. i.

of Adam Smith: it is an accumulated store of goods over and above what is required to satisfy current (*laufenden*) wants. In other words, *it is a surplus.* With profound insight, Professor Knies applies the term "capital" to this fundamental general conception of an *accumulated stock as a possession*, irrespective of the several specific ways it may be employed. Well might he ask, What right has any economist to claim the name "capital" exclusively for that portion of the stock which is devoted to production? The stock may be in the form of consumption goods, acquisitive goods, or production goods; but, so long as it *exists as a stock* over and above what is required for the satisfaction of current wants, it is fundamentally and essentially capital, without regard to any specific use to which it may be put.

Professor Knies's meaning, brought out by his analysis, is clear; but he was unfortunate in the phraseology of his definition. He defines capital as "the existing stock of goods (whether for consumption, acquisition, or production) which is available for the satisfaction of wants in the future." Professor v. Böhm-Bawerk, in his critique upon Knies's capital concept, instead of fairly and broadly interpreting the definition *in the light of the analysis*, has taken advantage of a technicality to reduce the distinction upon which Professor Knies's conception is founded to an absurdity. He has, as it were, taken Professor Knies's definition out of the context, and made his attack upon the use of the word "future." He represents that Professor Knies is apparently contrasting goods available for the satisfaction of "future" wants with goods available for the satisfaction of "present" wants, and then proceeds to show that all goods are for the satisfaction of "*future*" wants, and therefore that Professor Knies's conception of capital is identical with that of economic goods. No one can know better than Professor v. Böhm-

Bawerk that this interpretation does Professor Knies an injustice. The period which lies at the basis of Professor Knies's capital concept is evidently the "production period," which figures so prominently in Professor v. Böhm-Bawerk's theory of capital. Professor Knies, in his capital concept, is not contrasting goods for "present" with goods for "future" use, but, rather, *goods which are required for current consumption* during a production period with *an accumulated stock—a surplus*—of goods over and above what are required to satisfy current wants.

Though Professor Knies's analysis is vitiated by the unquestioned acceptance of the validity of Adam Smith's assumption, he came as near attaining the real capital concept as is possible on that basis. He saw clearly what Adam Smith and his successors did not see, that neither acquisitiveness nor productivity is an essential characteristic of the capital concept, and that the idea of a surplus as a possession is fundamental.

It has been made sufficiently plain that the true capital concept is not to be found in the direction of a category of concrete economic goods. It does not come within the purpose of the present article to go into the details of the fruitless search along that line. Enough has been said to show that the way is strewn with capital concepts, some broader, some narrower, some emphasizing one characteristic, some another, but no one of them capable of commanding general assent. So long as the assumption goes unchallenged that capital consists of a category of economic goods, and therefore that the only question to be determined is what goods are entitled to belong to the category, it is the writer's conviction that the capital controversy does not admit of solution. The immediate task, then, is clearly indicated; namely, to question Adam Smith's assumption that capital consists of a category of concrete goods, and thus consciously to attain the con-

ception of surplus wealth as a possession, expressible in terms of money, irrespective of the specific uses to which it may be put, as distinguished from Professor Knies's conception of an accumulated stock of goods (whether for production, acquisition, or consumption) as a possession. It is but a step from the one conception to the other; but it involves the placing back upon the main track of economic discussion the capital concept that belongs there: namely, the real capital concept,—the concept of Turgot.

Said Adam Smith:—

> Whoever derives his revenue from a fund which is his own must draw it either from his labor, from his stock, or from his land. The revenue derived from labor is called wages. That derived from stock, by the person who manages or employs it, is called profit. That derived by the person who does not employ it himself, but lends it to another, is called the interest or the use of money. It is the compensation which the borrower pays to the lender for the profit which he has an opportunity of making by the use of the money.[1]

Do we not find in the above passage an unconscious result of a fine distinction? It is seemingly intuitively made, as in popular speech. The capitalist lends money, while the entrepreneur uses "stock." The capitalist gets pay for the use of money; while the entrepreneur is able to make the payment by reason of the profit which he derives from the materials, machines, tools, etc., that he buys with the money. This means that, in the hands of the man whose income is derived from loans, capital is treated as a value, an abstract quantity of wealth; while in the hands of the entrepreneur it is regarded concretely as a mass of commodities that aid production. Had Adam Smith made this analysis consciously, and followed it to its logical conclusion, the Turgot capital concept would have been left upon the main track of economic discussion there would

[1] *Wealth of Nations*, vol. i. Book I. chap. vi.

have ensued no capital controversy, and the way would have been prepared for a speedy solution of the problem of distribution.

Economic science, however, was left to grope its way to the point of trying to do consciously what Adam Smith, in the passage cited, did unconsciously; namely, to distinguish between a *stock* consisting of concrete economic goods and a *capital* consisting of surplus wealth, expressible in terms of money. Ricardo's references to capital may be generally construed as indicating the concrete use of the term, though in some cases the popular and abstract meaning is evidently in the author's mind. When he speaks of "two different trades in which equal capitals are employed"[1] or of a "capital of £20,000"[2] or says that "capital would flow to the most profitable employment,"[3] he uses the popular and abstract concept. John Stuart Mill defines capital as "a stock previously accumulated of the products of former labor,"[4] and then proceeds to criticise persons "wholly unused to reflect" for supposing that capital is "synonymous with money." He makes no analysis in quest of the idea at the basis of the popular supposition. Yet in the same immediate connection he approaches the popular conception of capital as a sum expressible in money, which is invested in an ever-changing list of commodities, and, finally, actually speaks of the capital of the country as a "sum of values." These are simply illustrations of what is constantly recurring throughout the works of those writers who, like Adam Smith, consciously define capital as a category of economic goods, and unconsciously employ it in the sense of a fund of surplus wealth, expressible in terms of money.

It is, however, in accounting for the genesis of capital

[1] Ricardo, *On the Principles of Political Economy and Taxation*, 2d edition, 1819, p. 36.

[2] Ibid., p. 34. [3] Ibid., pp. 38, 39.

[4] Mill, *Principles of Political Economy*, vol. i. chap. iv. § 1.

that these writers fall into the abstract use of the term most frequently. It is customary for them to attribute the genesis of capital to "saving," "self-denial," "abstinence." Yet that concrete production goods, like tools, machines, and buildings, should originate in saving, is of course absurd; that these things, when once made, should be saved, and not utilized, is equally absurd. It is rather a portion of a man's income that is "saved,"—capitalized,—and as a fund of surplus wealth, expressible in terms of money, is invested in instruments in place of current consumption goods. The instruments perish in the using, but their value is "saved." It is what Professor Clark calls the "unconscious lapse into the abstract use of the term"[1] "capital" that blinds these writers to what must otherwise have appeared to them an absurdity.

The brilliant French economist, Jean Baptiste Say, was perhaps the first, after the publication of the *Wealth of Nations*, to consciously employ the Turgot capital concept, which we have shown to be a fund of surplus wealth,—expressible in terms of money,—irrespective of the specific use to which it may be put. In his *Catéchisme*, in reply to the question "What is capital?" Say answers, "It is an accumulated sum of values."[2] This must be looked upon as his definition, as Say's larger works, the *Traité* and the *Cours*, simply develop this proposition. He emphatically says that he does not mean by a "sum of values" a "sum of money." After enumerating the various prerequisites to production, such as tools, machines, implements, raw materials, buildings, money, etc., he says it is "the value of all these items" that constitutes what is called capital. Then he goes on to say that

[1] *Capital and its Earnings*, Publications of American Economic Association, vol. iii. p. 97.

[2] Say, *Catéchisme d'Économie Politique*, 3d edition Paris, 1826, p. 23.

"the capital of a nation is made up of the sum total of private capitals,"[1] and that but a trifling part of it is invested in the form of money. Capital is expressed in terms of money. He explicitly and repeatedly says that capital does not comprise material objects. It migrates through constantly changing forms of investment, appearing, vanishing, reappearing, and at the end of a production period it is unimpaired; for "capital consists not in this or that commodity or substance, but in its value,"[2] and "notwithstanding its frequent transmutations it is all the while the same capital." Further, Say consistently ascribes the origin and growth of capital to saving,[3] which he characterizes as the rescuing of value from destruction in final consumption. The value that comes into existence in the process of production must not all be permitted to go out of existence in the process of consumption: a portion of it must be accumulated as a surplus. The particular form in which value is saved and accumulated is represented as a matter of indifference: the essential thing is that it be saved, that it exist.

It should be noted, further, that Say does not regard it as essential that the "accumulated sum of values" should be devoted to production or acquisition, in order to be called capital. It may be invested in durable consumption goods,[4] like houses and furniture, without forfeiting the title. In short, the specific use to which it may be put is a matter of indifference, so far as its claim to be called capital is concerned. It is enough that this "accumulated sum of values" exists as a possession.

It is of course only by an acknowledged metaphor that one can speak of "talents," "acquired abilities," or the "man himself," as a concrete investment of an "accumu-

[1] Say, *Cours Complet d'Économie Politique Pratique*, vol. i. chap. xi.

[2] Ibid., vol. i. chap. x.

[3] Ibid., vol. i. chap. xiii.

[4] Ibid., vol. i. p. 295; vol. iv. pp. 190–192.

lated sum of values," or capital; and, in doing so, Say[1] seems, for the time, to have lost his bearings. With this exception, it may be added that Say, *in the main*, employs the term "capital" in the sense of an "accumulated sum of values" invested in material objects.

The way had not as yet been prepared for the general recognition of the Turgot capital concept. The fundamental conceptions must first receive a more profound and scientific analysis than had thus far been accorded them.

That the renaissance of economic theory during the past twenty-five years, and the searching analyses to which the fundamental concepts have been subjected at the hands of Professor Karl Knies, the Austrian school, and certain American economists, would bear fruit in the theory of capital, was of course to be expected. No less than three German and two American writers have raised the standard of revolt against the concrete capital concept of Adam Smith and his disciples, and demand a return to the popular and practical concept of business life. It remains for us to review this recent movement, which seems destined, ultimately, to place the Turgot capital concept back upon the main track of economic discussion.

The small group[2] of German writers, who must be regarded as pioneers in this movement, includes the distinguished Austrian economist, Professor Carl Menger, whose position is clearly outlined in an article published

[1] In the writer's judgment, Say has not received fair treatment at the hands of his critics. Böhm-Bawerk does him an injustice in attributing to him no less than four contradictory readings of the conception of capital.

[2] Richard Hildebrand, *Die Theorie des Geldes*, Jena, 1883. Hildebrand's definition of capital may be translated as follows: "Capital consists only in certain sums of value, available for the purpose of acquisition or already actually devoted to acquisitive purposes, no matter in what form they happen momentarily and from time to time to be: capital does not consist in certain objects of value." Ludwig Kühnast, "Ueber den rechtlichen Begriff des Kapitals," *Beiträge zur Erläuterung des Deutschen Rechts*, xxviii. Jahrgang (1884); Carl Menger, "Zur Theorie des Kapitals," Conrad's *Jahrbücher*, 1888, Band 51, 1-49.

in Conrad's *Jahrbücher* in July, 1888. Every careful student of the theory of capital must agree with Professor Menger that the return to the real concept (*Realbegriff*) of capital offers the only avenue of escape out of the prevailing confusion, and that this concept can be found only by a study of those phenomena which, in practical business life, bear the name "capital." Professor Menger recognizes in the economic science of the present three fundamental conceptions (*Grundauffassungen*) to which the name "capital" has been given. He regards all other concepts as varieties or combinations of these three, to which alone he confines his critique. These fundamental conceptions are: (1) acquisitive goods, as opposed to a stock of goods for personal use; (2) inchoate goods, as opposed to consumption goods; (3) "products" devoted to further production, as opposed to natural agents and labor. He recognizes the scientific importance of these conceptions, which have resulted from profound analyses of economic phenomena; but he characterizes the application of the term "capital" to them as arbitrary and absolutely without justification,—as the very thing which can but vitiate their scientific usefulness. Professor Menger points out that in practical business life, as well as in jurisprudence, the term "capital" is applied to neither raw materials nor commodities, nor machines nor buildings, but only to sums of money (*Geldbeträge*),—not to every sum of money, but only to sums of money which are devoted to the acquisition of income. He makes it clear that the practical business man does not confound capital and money, though he always speaks of capital in terms of money. The practical man applies the name "capital" to (1) sums to be loaned at interest,—in this case actual sums of money, as money is the form in which loans are made; (2) sums available for the opening of any sort of productive undertaking,—here, again, actual sums

of money; (3) the fund of value expressed in terms of money, though not in the form of money, but invested, rather, in goods of another sort in connection with some industrial enterprise. The merchant conceives of his stock of goods, the manufacturer of his stock of materials, as a sum of money devoted to the acquisition of income,—as a capital. Whenever the practical man thinks of his business as an investment of capital, he has always in mind a fund of value, expressible in terms of money, and not a lot of concrete goods of varied technical character, like land, machines, materials, and workshops.

It is the writer's judgment that Professor Menger, in his analysis of the practical notion of capital in the business world, has laid too much emphasis upon the purpose of capital and too little upon its fundamental character, and has thus made the real conception narrower than it logically is. He leaves the impression that this fund of value expressible in terms of money is capital only when devoted to the purpose of acquiring an income (interest). The inference is that this fund of value, if invested by its owner in durable consumption goods, is capital so long as these goods are used as a means of securing an income expressed as a percentage upon their value, but ceases to be capital the moment they are used directly to satisfy his personal wants. Does the question whether or not a given sum of surplus wealth is capital *turn upon the use* to which it is put? Analysis reveals that the very marrow of the practical conception of capital is the idea of a surplus as a possession. The man who has surplus wealth expressible in terms of money *has* capital. Surplus wealth *is* capital: it does not first become capital the instant its owner decides to devote it to some acquisitive purpose. The specific use to which the capital is put is a matter of secondary moment, as Professor Knies has clearly shown. That it will be put

to that use which, in the capitalist's judgment, will be to his best advantage, we may rest assured. It may be loaned at interest, or invested in land or machines or merchant's stock, or a house either to rent or to be occupied by the capitalist, or a stock of provisions or what not; or it may lie idle in the form of money, while the capitalist is making up his mind how to invest it,—free capital. It may be made to assume each of these states in succession. In no case, however, does it cease to be capital until it ceases to exist as a surplus.

The definition of capital as a fund of surplus wealth as a possession, expressible in terms of money, is but the logical rounding out of the popular notion, and not a distortion of it. It is the legitimate function of analysis in economic science to make the vague and indefinite popular notion assume the clear and definite outlines of a scientific concept. Only in this way can popular notions be made the guide to scientific truth. With the emphasis placed upon the real nature of capital rather than upon its purpose, Professor Menger's construction of the real capital concept would become identical with that of Turgot.

The eminent American economist, Professor John B. Clark,[1] must also be regarded as a pioneer in the movement to bring economic science back to the conception of capital in practical life. His monograph entitled *Capital and its Earnings*, in which he first outlined his position, appeared in the Publications of the American Economic Association in May, 1888, anticipating Professor Menger's article by about two months. Unfortunately,

[1] *Capital and its Earnings*, Publications of American Economic Association, 1888, vol. iii. pp. 89-149; "The Genesis of Capital," 1893, *Yale Review*, vol. ii. pp. 302-315; "The Origin of Interest," 1895, *Quarterly Journal of Economics*, vol. ix. pp. 257-278; "Real Issues concerning Interest," 1895, *Quarterly Journal of Economics*, vol. x. pp. 98-102; *The Distribution of Wealth*, 1900.

Professor Clark's treatment of the subject, owing to a careless use of terms, lacks the definiteness that a scientific treatise should have. Janus-like, he seems to be looking at the same time back to the concrete capital concept of Adam Smith and his followers and forward in the direction of the common, practical conception of business life. He began by contrasting the two conceptions, calling the former "concrete capital" and the latter "abstract, or pure capital." In his later work, entitled *The Distribution of Wealth,* he calls the former concept "capital goods," and the latter simply "capital." This change in terminology would seem to indicate a growth in the writer's own thought, yet the designation "capital goods" betrays a reluctance still to cut loose from classical moorings. One would reasonably expect, however, to find the common, practical concept clearly defined, and the simple term "capital" consistently applied to it. Yet this is not the case. Nowhere has Professor Clark attempted anything like formal definition of the capital concept; has perhaps consciously and purposely avoided it. At best he has given us only descriptions, leaving the reader to formulate his own definitions. For all that, one is hardly prepared for what he finds. The ninth chapter of *The Distribution of Wealth* bears the caption "Capital and Capital-goods Contrasted." The second paragraph of this chapter opens as follows: "*Capital* consists of *instruments of production,* and these are always *concrete and material.* This fact is fundamental." The Italics are not his. If *this* is capital, one finds himself asking, What can "*capital-goods*" mean? At first, one is constrained to think there must have been a misprint: the writer must have meant "*capital-goods.*" Yet the marginal topic, "*Capital always concrete and material,*"[1] would seem to indicate otherwise. The mystery increases as one reads further:—

[1] *The Distribution of Wealth,* p. 116.

> The most distinctive single fact about what we have termed capital is the fact of permanence. It lasts; and it must last if industry is to be successful. . . . Yet you must destroy "*capital-goods*" in order not to fail. . . . "Capital-goods" not only *may* go to destruction, but *must* be destroyed, if industry is to be successful; and they must do so, in order that capital may last.[1]

The reader is given shortly to understand that by "*capital-goods*" concrete material instruments are meant, like land, machines, materials, workshops, etc.,—exactly the kind of things he had but just described capital to consist of; while *capital* does not consist in material things at all, but in a fund of value expressible in terms of money, though not actually embodied in money.

At times the contrast between *capital* and "*capital-goods*" is brought out in strong relief and the issue clearly drawn, as when "the common and practical conception of capital as a permanent fund of wealth, expressible in money,—though not actually embodied in money,"—is set over against "the conception of concrete goods, distinguishable from others by reason of the place that they occupy in the order of industrial phenomena."[2] But when again emphasis is repeatedly laid upon the fact that capital is always "embodied" in "capital-goods," and should not be thought of apart from its material embodiment, that "it is not an abstraction, but a material entity," it seems as though, in the author's thought, the two conceptions had merged into one and capital had become, as Professor Carver[3] puts it in his critique, simply the quantitative measure of "capital-goods."

1 *The Distribution of Wealth*, p. 117. Professor Clark's discussion of capital is still further befogged by a loose use of the term "wealth," which he defines as concrete goods "objective to the user, material, useful, and appropriable," and then employs in an entirely different sense, that of a *quantum* of value expressible in terms of money,—leaving the reader to take the mean ing of the term from the context. See *Quarterly Journal of Economics*, vol. xv. pp. 240–242.

2 "Genesis of Capital," *Yale Review*, vol. ii. p. 306.

3 *Quarterly Journal of Economics*, vol. xv. p. 590.

One is brought inevitably to the conclusion that, after all, the real obscurity in Professor Clark's analysis is directly traceable to the use of the term "*capital-goods*." Why call production goods, comprising land, machines, materials, workshops, merchant's stock, and what not, "capital-goods"? Is it because these things have been *erroneously* called capital in economic literature? Manifestly not, as in that case they have forfeited their claim to the title, and Professor Clark has repeatedly said and implied as much. It must be, then, because production goods are always, in the author's thought, the embodiment of capital.

The question at once arises, Is Professor Clark's conception of capital, then, the "common and practical one"? Does the business man conceive of capital as a fund of wealth expressible in terms of money, though not embodied in money, but embodied, rather, in production goods? Evidently, that, and more. Capital, as the business man conceives it, is, to be sure, expressible in terms of money; but it comprises the whole fund of surplus wealth *as a possession*, in whatever form it may happen, momentarily, to be. It may be in the form of durable consumption goods, a stock of perishable consumption goods, or actual money, as well as in production goods. A construction of the capital concept, which would limit it to a specific use like production, is manifestly arbitrary, and utterly without justification in etymology or popular usage. As already said, the construction of the common and practical concept of capital must take cognizance of the *real nature* of the economic phenomenon to which in practical life that name is given rather than any specific purpose to which a portion of capital may momentarily—or permanently, for that matter—be applied.

It may be that Professor Clark did not purpose, in any of his published works, to give a complete analysis of the

"common and practical concept of capital." It may have been his intention merely to bring out clearly the nature of that concept in one particular direction; namely, production. In that case it must be acknowledged that his method is a faulty one, and has been the occasion of much misunderstanding and fruitless discussion. If the brilliant discussion which the publication of Professor v. Böhm-Bawerk's *Kapital und Kapitalzins* provoked has proved anything conclusively, it is certainly this: that the definition of the nature and limits of the capital concept is a prerequisite to a correct theory of interest. Our analysis has revealed that capital is an individual concept, though it works socially. Social capital is a misnomer, as Professor Menger has shown. A correct theory of interest must explain the earnings of capital in the sense of surplus wealth as a possession, and not simply of a particular portion of it. Is it too much to hope that the common and practical concept of capital here presented may be conducive to the attainment of such a theory?

In an able and suggestive critical review of "Recent Discussion of the Capital Concept," Professor Fetter[1] has presented "a restatement of the capital concept," which to the writer of this article seems utterly illogical and yet not altogether devoid of significance to the movement under consideration. Professor Fetter clearly belongs to the revolt against the capital concept of Adam Smith and his successors, and has come into touch with the common and practical concept, in so far as he has been led to adopt the money form of expression for capital. In his endeavor to avoid, on the one side, the danger of "over-abstraction" [2] with which he charges Professor Clark, and, on the other, the embarrassment of having two capital concepts

[1] "Recent Discussion of the Capital Concept," *Quarterly Journal of Economics*, vol. xv. pp. 1-45.

[2] *Quarterly Journal of Economics*, vol. xv. p. 9.

for which he criticises Professor v. Böhm-Bawerk, he decided that "in the capital concept must be united both the thought of concrete things and that of their value."[1] The avowed[2] purpose is to bring the competing concepts—on the one side, that capital consists of concrete goods, and, on the other, that it consists of the value of goods—into harmony by uniting them into a single concept.

The attempt certainly has all the charm of novelty. The following serves as a preliminary definition: "Capital is an aspect of material things, or, better, it consists of material things considered in one aspect,—their market value."[3] Professor Fetter then introduces the term "wealth," and, after defining it arbitrarily as synonymous with economic goods, restates his definition of capital in terms of wealth.

> Wealth and capital [he says] consist of *precisely the same things*. Wealth is the popular expression for goods the exact valuation of which is not stated. Capital is merely the ordinary market value expression of wealth. . . . Capital is economic wealth (goods) whose quantity is expressed in a general unit of value.[4]

These extracts from Professor Fetter's article clearly reveal the impracticability of the task undertaken. It is logically impossible to define capital, at the same time, both in terms of concrete goods and value; for the two conceptions are not identical, the two terms are not synonymous. Economic goods and value are two fundamentally distinct conceptions. Were that not the case, Professor Fetter would hardly have found, in economic literature, the two competing conceptions of capital which he proposes to harmonize. A specific *concrete* thing, then, cannot be measured and expressed in terms of an *abstract* unit of value. Only value can be quantitatively expressed in terms of a unit of value. If capital, then. is commonly

[1] *Quarterly Journal of Economics*, vol. xv. p. 40. [2] Ibid., p. 44.
[3] Ibid., p. 41. [4] Ibid., pp. 42–44.

expressed quantitatively in terms of a unit of value, must not capital be a sum of value—an abstraction, if you will—rather than a specific concrete good or a group of such goods? We have here all the parts of a syllogism, as follows:—

*Major premise.*—A *quantum* of value is, alone, expressible in terms of a unit of value.

*Minor premise.*—In a money economy, capital is quantitatively expressible in terms of a unit of value.

*Conclusion.*—In a money economy, capital is a *quantum* of value.

Professor Fetter is, then, logically constrained either to choose between the two concepts or to retain them both, as two fundamentally distinct conceptions. To call them both by the same name does not make them identical, but only creates confusion, as Professor Fetter's article has clearly shown. Would it not manifestly conduce to clear thinking and sound theory to call the concrete concept *production goods* and the abstract concept *capital?*

Unfortunately, Professor Fetter's discussion is vitiated by the assumption of a standpoint which, to the writer, seems arbitrary and purely academic. He proposes to ignore a fundamental distinction in actual life, which has become the basis of the two main logical divisions of economic science; namely, Production and Consumption. For him consumption does not exist as a distinct process, coordinate with the process of production. The line of demarcation between them vanishes, and with it the classification of economic goods into "consumption goods" and "production goods." With the merging of the two processes into one continuous productive process, the two classes of economic goods become merged into one all-embracing category of "production goods." Satisfactions are regarded as the only true product, and are to be called "economic goods." Economic goods—all of

them production goods—are to be called wealth, and become capital "either singly or in groups," when their value is expressed in a general unit of value. To eat one's dinner is to produce, as eating is but the final stage in the productive process: the articles of food upon the table are production goods, and, when expressed quantitatively in terms of a general unit of value, are capital. What a perversion of economic science, whose purpose it is, in Professor v. Böhm-Bawerk's phrase, "to hold up the mirror to the world of reality"!

The results of our inquiry may now be summarized,—both the positive conclusions reached in the first part of the article and the outcome of the historical and critical discussion, in the second part.

In order to prepare the way for the analysis of the real capital concept, attention was called to the fundamental distinction between "consumption goods" and "production goods," and to the contrast between the direct method of production and the indirect method, to which Professor v. Böhm-Bawerk has given the name "capitalistic production."

Then the proposition was advanced that the name "capital" rightfully belongs to the *underlying basis* of capitalistic production rather than to any specific outward manifestation of it. This was found to be *surplus wealth as a possession,* expressible—in a money economy—in terms of money.

Substantial grounds were then given for the belief that the conception of *surplus wealth as a possession* is clearly entitled to be called capital, namely: *first,* it is the common and practical conception of capital; *second,* the concept is etymologically entitled to the name; and, *third,* its claim to the name is substantiated by the principles laid down by Professor v. Böhm-Bawerk for such cases.

It was then pointed out that Turgot was historically

the first economist to apply the term "capital" to the conception of *surplus wealth as a possession*, expressible in terms of money, irrespective of the technical goods in which it might, momentarily, be invested and of the specific use to which it might be put.

It was next shown that Adam Smith introduced into economic science a brand-new capital concept. He assumed, *first*, that capital consists of concrete goods, and, *second*, that the specific use to which they are put is vital to the conception, and thus introduced a fruitless controversy as to the scope of the capital concept. In this controversy the fundamental conception of a *surplus as a possession* was lost sight of completely, until Professor Karl Knies called attention to its fundamental character and made it the basis of his definition of capital, showing that the specific use to which goods may be put is a matter of only secondary importance.

It was now pointed out that the next task was to bring economic science to consciously conceive of this *surplus* as a fund of value as a possession, expressible in terms of money, as distinguished from a "stock" of concrete goods.

Though all economists were in the habit of unconsciously using the term "capital" in the abstract sense, and Say did so consciously, no persistent effort was made to press upon economic science the claims of the abstract conception, until the renaissance of economic theory had both prepared the way for and demonstrated the necessity of a deeper analysis of the capital concept.

In the remaining portion of the article it was shown that Professors Menger, Clark, and Fetter, in presenting the claims of the value concept, have fallen into the error of Adam Smith and his successors, in emphasizing the *purpose*—whether of acquisition or production—as vital to the concept itself. They do not seem to have consciously

grasped the conception of *surplus wealth as a possession,* expressible in terms of money, irrespective of any specific use to which it may be put.

This is the real capital concept. This article has been written to direct attention, as its title indicates, to the name "capital." It is believed that the cause of sound economic theory will be best served by reserving the name "capital" exclusively for this conception.

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